



The Law Society of
Upper Canada

Barreau
du Haut-Canada

2003 e-MAR

Annual Report
2003
Financial
Statements



The Law Society of Upper Canada

Annual General Meeting, 2004

WEDNESDAY, MAY 12, 2004

AT 5:15 P.M.

OSGOODE HALL, TORONTO

ORDER OF BUSINESS

Minutes of the previous Annual General Meeting

Report of the work of the Society and
the committees of Convocation

Presentation of the audited financial statements

Matters of professional interest that are related
to the work of the Society

This report is available on the Law Society
of Upper Canada Web site: www.lsuc.on.ca.

For additional copies, please contact the
Communications and Public Affairs Department
at 416-947-5220.

2-14	GENERAL FUND <i>Management Discussion and Analysis, Auditors' Report, Financial Statements and Notes</i>
15-21	LAWYERS FUND FOR CLIENT COMPENSATION <i>Management Discussion and Analysis, Auditors' Report, Financial Statements and Notes</i>
22-33	ERRORS AND OMISSIONS INSURANCE FUND <i>Management Discussion and Analysis, Auditors' Report, Actuary's Report, Financial Statements and Notes</i>
34-43	LIBRARYCO INC. <i>Management Discussion and Analysis, Auditors' Report, Financial Statements and Notes</i>



Management Discussion and Analysis

The Society's General Fund comprises its unrestricted fund, funds restricted by Convocation for special purposes and endowment funds held in trust. The Capital Fund, which records transactions of a capital nature, is one of the funds restricted by Convocation. The Society's annual membership fee is based on the financial requirements of the restricted and unrestricted funds.

BALANCE SHEET

Cash and short-term investments

Cash and short-term investments have increased by approximately \$1.3 million from the 2002 year-end to \$26.2 million. \$10 million will be invested in a new long-term portfolio in 2004. The short-term investments include government backed securities and money market instruments issued by major Canadian Banks.

Deferred revenue

Deferred revenue of \$1.9 million has decreased by \$2.6 million from 2002. It is predominantly 2004 membership fees received in 2003.

Unclaimed trust funds

Unclaimed trust funds continue to increase with the current balance at \$729,000. These are trust monies turned over to the Society by members who are unable to locate the person or persons to whom the monies are owed. By statute, the Society administers these funds, in perpetuity, with the net income from the funds transferred to the Law Foundation of Ontario annually. No claims have been made against the fund to date.

STATEMENT OF REVENUES AND EXPENSES

Law Society operations generated a surplus of \$3.9 million in 2003.

Membership fees

Membership fees for 2003 are \$33.8 million, 5% less than 2002 as a result of a reduction in the annual general membership levy from \$1,328 to \$1,209 (9%), offset by the net increase in membership numbers of approximately 1,000.

Professional Development and Competence

In 2003, the Professional Development and Competence (PD&C) Department fulfilled its primary objective of addressing member needs to fulfill minimum expectations for professional development as set out in the Competence Mandate. Achieving this objective can be measured by the continued expansion of Law Society competence products and service offerings and increasing attendance at post-call education ("PCE") programs – the 38% increase in attendance in 2002 was followed by a 56% increase in attendance in 2003.

At \$11.2 million PD&C revenues have remained static with 2002. The registration cost for attending a program delivered electronically is significantly less than programs where physical attendance is

required and in 2003 half the programs were presented electronically compared to none in 2002. This has improved program affordability, accessibility, relevance and flexibility. The Bar Admission Course (BAC) enrollment and tuition fees were at the same levels as 2002.

The Law Society works co-operatively with other not-for-profit legal education providers in the provision of PCE products. We are able to tailor product lines to meet the demands of the market or adjust costs in the face of lower revenue expectations.

In 2003, increased participation in PCE resulted in increased variable costs particularly as developing flexible electronic delivery formats is more expensive than maintaining the more traditional learning formats. However, BAC expenses declined by more than 10% due to improvements in delivery resulting in total PD&C expenses of \$14.5 million being comparable on a year over year basis.

Professional Regulation

In 2003, the focus of the Professional Regulation Division was to analyse and improve its underlying business processes, with a view to improve efficiency, effectiveness, transparency, accountability and timeliness. As planned, the Division's business process report was completed. Resulting improvements included the development of a staff procedures manual, templates, targets and measures, and two new departments, Intake and also Monitoring and Enforcement. The remainder of the business process plan will be implemented in 2004 along with a case management system.

The increase in the expenditures for Professional Regulation from \$8.3 million in 2002 to \$9.0 million in 2003 was due to the above initiatives, divisional restructuring and the additional expenses incurred as a result of the increasing numbers of mortgage fraud investigations which are unusually resource intensive. The organizational changes made in 2003 are expected to lead to more predictable budget performance in future years, and close alignment with production targets. The reorganization, with the establishment of an enforcement section is also expected to result in improved cost recoveries.

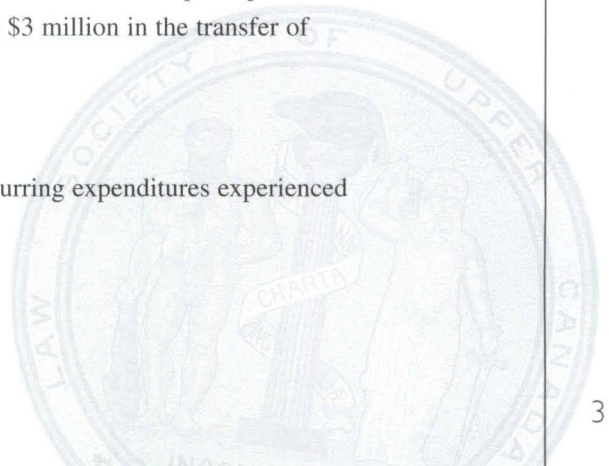
The Division's objective is to respond to allegations of misconduct or incapacity on the part of lawyers, and to the extent that it is possible, to deter other lawyers from engaging in similar conduct. The Division will be working with PD&C to develop opportunities for support or education in practice areas which the regulatory function has identified as susceptible to problems.

Investment income

Investment income has increased to \$4.0 million from \$3.3 million because of increased principal balances over the year, improved returns and an increase of \$400,000 to \$3 million in the transfer of income from the Errors and Omissions Fund.

Other

The decrease in other expenses of \$1.4 million is attributable to non-recurring expenditures experienced in 2002 such as litigation and reorganization costs.





Auditors' Report

TO THE MEMBERS OF THE LAW SOCIETY OF UPPER CANADA,

We have audited the balance sheet of THE LAW SOCIETY OF UPPER CANADA – GENERAL FUND as at December 31, 2003 and the statements of revenues and expenses, changes in fund balances and cash flows for the year then ended. These financial statements are the responsibility of the Society's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the General Fund as at December 31, 2003 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario

February 6, 2004

Balance Sheet

Stated in thousands of dollars

As at December 31

	2003	2002
ASSETS		
Current Assets		
Cash and short-term investments	26,245	24,928
Accounts receivable (note 3)	1,221	1,952
Prepaid expenses	309	173
Total current assets	27,775	27,053
Capital assets (note 4)	16,965	17,345
Total Assets	44,740	44,398
LIABILITIES AND FUND BALANCES		
Current Liabilities		
Accounts payable and accrued liabilities	6,614	7,138
Deferred revenue	1,891	4,514
Total current liabilities	8,505	11,652
Unclaimed trust funds (note 5)	729	435
Total Liabilities	9,234	12,087
RESTRICTED FUND BALANCES		
Capital allocation	9,383	5,605
Invested in capital assets	16,965	17,345
County libraries	230	553
Repayable allowances	325	338
Endowments	498	495
Special projects	130	—
Working capital reserve	7,975	7,975
Total Fund Balances	35,506	32,311
Total Liabilities and Fund Balances	44,740	44,398

See accompanying notes

On behalf of Convocation

Frank Manion

Treasurer

Clayton Ruby

Chair of Finance and Audit Committee





Statement of Revenues and Expenses

Stated in thousands of dollars

Year ended December 31

	2003			2002		
	Unrestricted Fund	Restricted Funds	Total	Unrestricted Fund	Restricted Funds	Total
REVENUES						
Membership fees	26,348	7,540	33,888	27,981	7,757	35,738
Professional development and competence	11,253	—	11,253	11,475	—	11,475
Investment income	4,011	15	4,026	3,336	14	3,350
Other (note 6)	4,491	37	4,528	4,535	—	4,535
Total revenues	46,103	7,592	53,695	47,327	7,771	55,098
EXPENSES						
Professional development and competence	14,551	—	14,551	14,645	—	14,645
Professional regulation	9,029	—	9,029	8,340	—	8,340
Administrative	7,338	—	7,338	7,255	—	7,255
Other (note 7)	4,025	—	4,025	5,435	—	5,435
Client service centre	3,383	—	3,383	3,137	—	3,137
Facilities	2,940	—	2,940	2,883	—	2,883
Policy and legal affairs	1,983	—	1,983	1,757	—	1,757
Communications	1,347	—	1,347	1,238	—	1,238
Equity	864	—	864	752	—	752
Tribunals	503	—	503	335	—	335
Capital allocation fund	—	815	815	—	1,341	1,341
Invested in capital assets — amortization	—	1,485	1,485	—	1,698	1,698
County libraries fund	—	5,795	5,795	—	5,408	5,408
Repayable allowances fund	—	114	114	—	209	209
Endowments	—	12	12	—	23	23
Special projects	—	70	70	—	—	—
Total expenses	45,963	8,291	54,254	45,777	8,679	54,456
Less: Expenses Allocated to Lawyers Fund for Client Compensation (note 1)	3,754	—	3,754	3,129	—	3,129
Net expenses	42,209	8,291	50,500	42,648	8,679	51,327
Surplus (deficit)	3,894	(699)	3,195	4,679	(908)	3,771

See accompanying notes

Statement of Changes in Fund Balances

Stated in thousands of dollars

Year Ended December 31

	2003										2002
	RESTRICTED FUNDS										
	Unrestricted Fund	Capital Allocation	Invested in Capital Assets	County Libraries	Repayable Allowances	Endowments	Special Projects	Working Capital Reserve	Total Restricted Funds	Total	Total
Fund balances, beginning of year	–	5,605	17,345	553	338	495	–	7,975	32,311	32,311	28,540
Revenues	46,103	2,104	–	5,472	1	15	–	–	7,592	53,695	55,098
Expenses	42,209	815	1,485	5,795	114	12	70	–	8,291	50,500	51,327
Surplus (Deficit)	3,894	1,289	(1,485)	(323)	(113)	3	(70)	–	(699)	3,195	3,771
Interfund transfers											
Transfer to capital allocation	(3,594)	3,594	–	–	–	–	–	–	3,594	–	–
Asset capitalization	–	(1,105)	1,105	–	–	–	–	–	–	–	–
Transfer to special projects	(200)	–	–	–	–	–	200	–	200	–	–
Transfer to repayable allowances	(100)	–	–	–	100	–	–	–	100	–	–
Total interfund transfers	(3,894)	2,489	1,105	–	100	–	200	–	3,894	–	–
Fund balances, end of year	–	9,383	16,965	230	325	498	130	7,975	35,506	35,506	32,311

See accompanying notes

GENERAL FUND

Financial Statements

Statement of Cash Flows

*Stated in thousands of dollars**Year ended December 31*

	2003	2002
OPERATING ACTIVITIES		
General fund surplus	3,195	3,771
Item not affecting cash:		
Amortization of capital assets	1,485	1,698
Other operating sources (uses) of cash:		
Accounts receivable	731	(392)
Prepaid expenses	(136)	39
Accounts payable and accrued liabilities	(524)	737
Deferred revenue	(2,623)	2,557
Fund contribution – unclaimed trusts	294	435
Total operating activities	2,422	8,845
INVESTING ACTIVITY		
Capital asset additions	(1,105)	(1,635)
Net increase in cash and short-term investments during the year	1,317	7,210
Cash and short-term investments, beginning of year	24,928	17,718
Cash and short-term investments, end of year	26,245	24,928

See accompanying notes

Notes to Financial Statements

For the year ended December 31, 2003

(Stated in whole dollars except where indicated)

1. Description of Fund

The Law Society of Upper Canada (the "Society") was founded in 1797 and was incorporated in 1822 with the enactment of the *Law Society Act*. The Society exists to govern the legal profession in the public interest. This is achieved by ensuring that the people of Ontario are served by lawyers who meet high standards of learning, competence and professional conduct and by upholding the independence, integrity and honour of the legal profession, for the purpose of advancing the cause of justice and the rule of law. The governing body of the Society, which is known as Convocation, carries out this mandate.

The *Law Society Amendment Act 1998* received royal assent in December 1998 and came into force on February 1, 1999. This Act makes substantive and important amendments to the *Law Society Act*, including a restructuring scheme of professional governance based on the authority in the statute. The *Law Society Amendment Act, 1998*, authorizes the Society to make regulations, by-laws and rules of practice and procedure as a means of governing all proceedings described in the Act.

The Society is not subject to income or capital taxes because it is a not-for-profit corporation. These financial statements represent the financial position and operations of the Law Society of Upper Canada – General Fund, which includes certain internally restricted funds, and do not purport to represent all assets and liabilities under the control of the Society.

Separate financial statements have been prepared for the following related entities, which have not been consolidated into the General Fund statements:

Lawyers Fund for Client Compensation

The Society maintains the Lawyers Fund for Client Compensation ("Compensation Fund") pursuant to section 51 of the *Law Society Act* to relieve or mitigate loss sustained by any person in consequence of dishonesty on the part of any member in connection with such member's law practice or in connection with any trust of which the member was or is a trustee. Members' annual fees and investment income finance the Compensation Fund. The Compensation Fund reports fees collected by the General Fund as revenues. The Compensation Fund reimburses the General Fund for certain administrative expenses, spot audit expenses and a portion of the costs of operating the investigation and discipline functions of the Society. These amounted in 2003 to \$3,754,000 (2002 – \$3,129,000).

Errors & Omissions Insurance Fund and Lawyers' Professional Indemnity Company

The Society provides professional liability insurance to the legal profession through the Errors and Omissions Insurance Fund ("E&O Fund") and the Lawyers' Professional Indemnity Company ("LAWPRO"). The E&O Fund was originally set up in the Society's accounts to record insurance claims and expenses and related levies and their investment. Prior to July 1, 1990 various insurance carriers underwrote the Errors and Omissions Insurance program. LAWPRO took over underwriting the program commencing July 1, 1990. LAWPRO, a wholly owned subsidiary of the Society, was incorporated in 1990 and is licensed to provide lawyer's professional liability and title insurance. On an annual basis the



E&O Fund provides the General Fund with income derived from its surplus earnings. This income, reported as Investment Income of the General Fund, amounted in 2003 to \$3,000,000 (2002 – \$2,600,000).

LibraryCo Inc.

LibraryCo Inc. is a wholly owned, not-for-profit subsidiary of the Society. LibraryCo Inc. was originally incorporated under the *Business Corporations Act* of Ontario on December 20, 2000 and was succeeded by another corporation of the same name on April 12, 2001. The Corporation issued 100 voting Common Shares to the Society for \$100 and 100 Special Shares to the County and District Law Presidents' Association for \$100. The holders of the Special Shares are entitled to elect one director.

The Society levies and collects funds for county and district law library purposes. Convocation internally restricts these funds for use by these law libraries to carry out their annual operations and any special projects approved by Convocation. LibraryCo Inc. was established to administer this funding on behalf of the Society and to develop policies, procedures, guidelines and standards for the delivery of county law library services across Ontario.

Law Society Foundation

The Law Society Foundation ("LSF"), a registered charity, was incorporated by Letters Patent in October 1962. The objects of the LSF are to foster, encourage and promote legal education in Ontario, provide financial assistance to law students in Ontario, restore and preserve land and buildings of historical significance to Canada's legal heritage, receive gifts of muniments and legal memorabilia of interest and significance to Canada's legal heritage, to maintain a collection of gifts of books and other written material for use by educational institutions in Canada and to receive donations, and maintain a fund for the relief of poverty by providing meals to persons in need. The Society provides facilities, administration, accounting, security and certain other services at no cost to the LSF.

The Law Foundation of Ontario

The Law Foundation of Ontario ("LFO") was created to receive interest accruing on monies held in lawyers' mixed trust accounts and to establish and maintain a fund to be used for the purposes of legal education and legal research, legal aid and the establishment, maintenance and operation of law libraries. During 2003, the LFO contributed to the General Fund of the Society \$1,062,900 (2002 – \$1,300,000) for the operation of the Bar Admission Course and \$100,000 (2002 – \$45,000) for legal heritage programs.

2. Significant Accounting Policies

Basis of presentation

The financial statements have been prepared in accordance with the accounting standards for not-for-profit organizations published by the Canadian Institute of Chartered Accountants using the restricted fund method of reporting revenues.

Description of funds

The *Unrestricted Fund* accounts for the Society's program delivery and administrative activities. This fund reports unrestricted resources.

The *Capital Allocation Fund* is maintained to provide a source of funds for the acquisition and maintenance of the Society's capital assets. These include buildings and major equipment including

computers. Amounts of assets capitalized, according to the Society's Capital Asset policy, are transferred to the Invested in Capital Assets Fund. Expenditures not capitalized are expended in the Capital Allocation Fund. As at December 31, 2003 the balance is \$9,383,000 (2002 – \$5,605,000). This balance is available to finance a major building renovation beginning in 2004.

The *Invested in Capital Assets Fund* records transactions related to the Society's capital assets, specifically acquisitions, amortization and disposals. As at December 31, 2003 the balance is \$16,965,000 (2002 – \$17,345,000)

The *County Libraries Fund* accumulates funds raised by the Society for county library purposes and these funds are accounted for as a Restricted Fund of the Society. The Society remits amounts to LibraryCo Inc. on a predetermined basis. On an annual basis, amounts collected that exceed the current year requirements are held by the Society and accounted for in the fund balance. At December 31, 2003 the fund balance was \$230,000 (2002 – \$553,000). This amount is available to reduce the amount levied on the membership in 2004.

The *Repayable Allowances Fund* provides students with funding for tuition and living expenses and is based on a student's ability to repay the grant within a specified period of time following the student's non-participation in the Bar Admission Course. A staff committee reviews and decides on applications according to guidelines set out by Convocation. At December 31, 2003, the Fund Balance was \$325,000 (2002 – \$338,000).

The Society administers two *Endowment Funds*. The Law Society Trust was established in accordance with the terms of the endowments so that the Society can award prizes, bursaries and gifts to deserving students in the Bar Admission Course. The J. Shirley Denison Fund was established to provide relief and assistance to members and former members who find themselves in difficult financial circumstances. Contributions for endowments are recognized as revenue in the Endowment Funds. For 2003, no funds were contributed for endowment purposes. At December 31, 2003, the Funds Balances totalled \$498,000 (2002 – \$495,000).

The *Special Projects Fund* is maintained to ensure that financing is available for Convocation's ongoing special projects. In 2003, Convocation established the Sole Practitioner and Small Firm Task Force and allocated \$200,000 to complete its work. The balance at December 31, 2003 is \$130,000.

The *Working Capital Reserve* is maintained to ensure adequate cash reserves for the continuous financing of the Society's operations. This fund is internally restricted by Convocation and its balance is sufficient to provide for the Society's operating expenses for up to two months. As at December 31, 2003 the balance is \$7,975,000 (2002 – \$7,975,000).

Cash and short-term investments

Cash and short-term investments are amounts on deposit and invested in short-term (less than one year) investment vehicles according to the Society's investment policy. Short-term investments are stated at the lower of cost and market value. Investment income, except income earned on resources held for endowment, is retained in and reported by the Unrestricted Fund.

Capital assets

Assets are capitalized and subject to amortization when they are determined to have a minimum useful life of three years and an acquisition cost of \$10,000 for equipment, furniture, and computer equipment, \$25,000 for computer software and \$25,000 for building improvements. Capital Assets are presented at cost net of accumulated amortization and grants. For purposes of calculating the first year's



amortization, all capital assets are deemed to be acquired, put into service, or completed on July 1st. Amortization is charged to expenses on a straight-line basis over the estimated useful lives of the assets as follows:

Buildings	30 years
Building improvements	10 years
Furniture, equipment and computer hardware and software	3 to 5 years

Revenue recognition

Restricted contributions related to the general operations are recognized as revenue of the General Fund in the year in which the related expenses are incurred. All other restricted contributions are recognized as revenue of the appropriate restricted fund. Unrestricted contributions are recognized as revenue of the Unrestricted Fund in the year received or receivable if the amount can be reasonably estimated and collection is reasonably assured.

Collections

The Society owns a collection of legal research and reference material as well as a collection of portraits and sculptures. The cost of additions to the collections is expensed as incurred. No value is recorded in these financial statements for donated items.

Volunteer services

The work of the Society is dependent on the voluntary services of the elected Benchers and other members of the profession. These services are received gratuitously; therefore, no value has been included in these financial statements.

Financial instruments

The estimated fair values of cash and short-term investments, accounts receivable, prepaid expenses, accounts payable, accrued liabilities and deferred revenue approximate their carrying amounts in the financial statements due to the relatively short period to maturity of these instruments.

Measurement uncertainty

The preparation of the financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingencies at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Accounts Receivable

Included in accounts receivable are certain amounts receivable from related parties as follows:

	2003	2002
Lawyers Fund for Client Compensation	164,620	741,558
LibraryCo Inc.	7,680	82,883
The Law Society Foundation	11,541	-
The Law Foundation of Ontario	320,607	357,900
Lawyers' Professional Indemnity Company	21,223	17,200

4. Capital Assets

As at December 31, 2003

(\$000's)	Cost	Accumulated Amortization	Net
Land and buildings	27,946	16,063	11,883
Building improvements	6,153	2,085	4,068
Furniture, equipment and computer hardware and software	3,356	2,342	1,014
	37,455	20,490	16,965

As at December 31, 2002

(\$000's)	Cost	Accumulated Amortization	Net
Land and buildings	27,946	15,472	12,474
Building improvements	5,466	1,680	3,786
Furniture, equipment and computer hardware and software	2,937	1,852	1,085
	36,349	19,004	17,345

5. Unclaimed Trust Funds

Section 59.6 of the *Law Society Act* permits a member who has held money in trust for or on account of a person for a period of at least two years to apply in accordance with the by-laws for permission to pay the money to the Society. Money paid to the Society is held in trust in perpetuity for the purpose of satisfying the claims of the persons who are entitled to the money. Subject to certain provisions in the Act which enable the Society to recover its expenses associated with maintaining these funds, all income from the money held in trust shall be paid to the *Law Foundation of Ontario*. Money held in trust amounts to \$729,000 (2002 – \$435,000).

6. Other Revenue

Included in other revenue is income from the Ontario Reports, catering, the Lawyer Referral Service, specialist certification and other miscellaneous revenues.

7. Other Expenses

Included in other expenses are payments to the Federation of Law Societies, County and District Law Presidents' Association, insurance, professional fees, bench/governance related disbursements, termination payments, special projects fully funded within the year, and other corporate expenses.

8. Pension Plan

The Society maintains a defined contribution plan for all eligible employees of the Society. The Society matches its employees' contributions to the plan. The Society's General Fund pension expense in 2003 amounted to \$942,538 (2002 – \$800,359).



9. Commitments

The Society is committed to monthly lease payments for property and equipment under leases having various terms up to the end of April 2005. Aggregate minimum monthly payments over the next two years are as follows:

Year	\$000's
2004	326
2005	113
Total	439

10. Contingent Liabilities

A number of claims or potential claims are pending against the Society. It is not possible for the Society to predict with any certainty the outcomes of such claims or potential claims. Management is of the opinion that based on the information presently available, it is unlikely that any liability, to the extent not covered by insurance, would be material to the Society's financial position.

11. Comparative Figures

Certain of the prior year's comparative figures have been reclassified to conform to the current year's financial statement presentation.

Management Discussion and Analysis

The Lawyers Fund for Client Compensation has enjoyed a third consecutive year of moderate claims against the Fund. This has contributed to an increase of \$2.5 million in the Fund's year-end balance from \$14.9 million to \$17.4 million.

BALANCE SHEET

Cash and short-term investments

The Compensation Fund's balance sheet continues to strengthen after revenues exceeded expenses for the third year. Cash and short-term investments decreased by \$4 million to \$8.2 million due to a transfer of \$5 million to portfolio investments. The Compensation Fund's short-term investments are invested in bankers acceptances, Government of Canada T-bills and cash.

Portfolio investments

The Compensation Fund's portfolio investments of \$19.8 million are invested in high quality fixed income (83%) and equity (17%) products with a long-term investment horizon. The market value of the portfolio is \$20.4 million.

Reserve for unpaid grants

Based upon the actuarial valuation of the grant reserve, the reserve for unpaid grants has decreased by \$800,000 to \$9.8 million.

STATEMENT OF REVENUES AND EXPENSES AND CHANGE IN FUND BALANCE

Revenues

Membership fees

The Compensation Fund's claim experience in recent years has permitted a decrease in membership fees declining from \$290 per member in 2002 to \$280 per member in 2003. This decrease was offset by an increase in the number of members, leading to static total membership fees of \$7.8 million.

Investment income

The Compensation Fund's investment income in 2003 increased to \$1.3 million from \$542,000 because of capital gains and higher returns from the fixed income portfolio. 2002 investment income was reduced by a provision for decline in the value of equity investments of \$320,000.

Expenses

Grants

The net grants expense decreased from \$2.8 million in 2002 to \$1.7 million due to favourable developments on claims reported prior to 2003 and the resultant reduction in required reserves for these claims.

Other expenses

The Compensation Fund's operating expenses increased from 2002. In departments such as Spot Audit more complete staff complements allowed more complete development and implementation of departmental mandates.



Auditors' Report

TO THE MEMBERS OF THE LAW SOCIETY OF UPPER CANADA,

We have audited the balance sheet of THE LAW SOCIETY OF UPPER CANADA – LAWYERS FUND FOR CLIENT COMPENSATION as at December 31, 2003 and the statements of revenues and expenses and change in fund balance and of cash flows for the year then ended. These financial statements are the responsibility of the Society's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2003 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario

February 6, 2004

Balance Sheet

Stated in thousands of dollars

As at December 31

	2003	2002
ASSETS		
Current Assets		
Cash and short-term investments	8,222	12,230
Interest and other receivables	166	150
Total Current Assets	8,388	12,380
Portfolio investments		
(market value – \$20,362; 2002 – \$14,291)	19,829	13,973
Total Assets	28,217	26,353
LIABILITIES AND FUND BALANCE		
Accounts payable and accrued liabilities (note 4)	926	744
Reserve for unpaid grants (notes 2 and 3)	9,854	10,681
Total Liabilities	10,780	11,425
Fund Balance	17,437	14,928
Total Liabilities and Fund Balance	28,217	26,353

See accompanying notes

On behalf of Convocation

Frank Manuella

Treasurer

Clayton Ruby

Chair of Finance and Audit Committee





Statement of Revenues and Expenses and Change in Fund Balance

Stated in thousands of dollars

Year ended December 31

	2003	2002
REVENUES		
Membership fees	7,857	7,847
Investment income	1,287	542
Total revenues	9,144	8,389
EXPENSES		
Grants paid	2,701	1,321
(Decrease)/Increase in reserve for unpaid grants	(827)	1,479
Recoveries	(165)	(30)
Net grants expense	1,709	2,770
Spot audit	1,838	1,565
Share of investigation and discipline	1,046	1,021
Administrative	997	667
Insurance	495	535
Salaries and benefits	512	458
Claimants' counsel fees	29	51
Referees' and reporters' fees	9	9
Total expenses	6,635	7,076
Surplus	2,509	1,313
Fund balance, beginning of year	14,928	13,615
Fund balance, end of year	17,437	14,928

See accompanying notes

Statement of Cash Flows

Stated in thousands of dollars

Year ended December 31

	2003	2002
OPERATING ACTIVITIES		
Surplus	2,509	1,313
Items not affecting cash:		
(Decrease)/increase in reserve for unpaid grants	(827)	1,479
Provision for decline in value of portfolio investments	–	320
Other operating sources (uses) of cash:		
Interest and other receivables	(16)	(5)
Accounts payable and accrued liabilities	182	568
Total operating activities	1,848	3,675
FINANCING ACTIVITY		
Portfolio investments (net)	(5,856)	(549)
Net (decrease)/increase in cash and short-term investments during the year	(4,008)	3,126
Cash and short-term investments, beginning of year	12,230	9,104
Cash and short-term investments, end of year	8,222	12,230

See accompanying notes





Notes to Financial Statements

For the year ended December 31, 2003

(Stated in whole dollars except where indicated)

1. Description of Fund

The Lawyers Fund for Client Compensation (the "Fund") is maintained by the Law Society of Upper Canada (the "Society") pursuant to section 51 of the *Law Society Act* to relieve or mitigate loss sustained by any person in consequence of dishonesty on the part of any member in connection with such member's law practice or in connection with any trust of which the member was or is a trustee. The Fund is financed by members' annual fees and investment income.

The Fund is not subject to income or capital taxes because it is a fund of the Society, a not-for-profit corporation.

Certain services are provided by the General Fund of the Society to the Fund. The Fund reimburses the Society for certain administrative expenses, spot audit expenses and a portion of the costs of operating the investigation and discipline functions of the Society. The charges for the year amount to \$3,754,000 (2002 – \$3,129,000).

2. Significant Accounting Policies

Basis of presentation

The financial statements have been prepared in accordance with the accounting standards for not-for-profit organizations published by the Canadian Institute of Chartered Accountants, using the restricted fund method of reporting revenues. The Fund accounts for the program delivery, administration and payment of grants from the Fund. The Fund is restricted in use by the *Law Society Act*.

Cash and short-term investments

Cash and short-term investments are amounts on deposit and invested in short-term (less than one year) investment vehicles according to the Society's investment policy. Short-term investments are stated at the lower of cost and market value.

Portfolio investments

Portfolio investments are recorded at cost, net of amortization of premiums and discounts. Investments consist of a diversified portfolio of government bonds, corporate bonds and Canadian and U.S. equities, according to the Society's investment policy. Only if a loss in the value of an investment is other than a temporary decline is the investment written down to recognize the loss.

Grants

Pursuant to section 51(5) of the *Law Society Act*, the payment of grants from the Fund is at the discretion of Convocation, the governing body of the Society. Grants paid are subject to a \$100,000 limit per applicant. A reserve for unpaid grants is recorded as a liability on the balance sheet. This

reserve represents an estimate of the present value of grants to be paid for unprocessed claims and the associated administrative costs, as determined by an actuary. The related net grants expense represents grant payments during the year plus the current year experience gain/loss of the reserve for unpaid grants, net of recoveries. The Fund maintains insurance for cumulative claims in excess of \$15,000,000 to a maximum of \$25,000,000. On an annual basis, actuarial valuations are used to determine the appropriate levels of insurance that the Fund purchases.

Financial instruments

The estimated fair values of cash and short-term investments, interest and other receivables and accounts payable and accrued liabilities approximate their carrying amounts in the financial statements due to the relatively short period to maturity of these instruments.

3. Measurement Uncertainty

The valuation of unpaid grants anticipates the combined outcomes of events that are yet to occur. There is uncertainty inherent in any such estimations and therefore a limitation upon the accuracy of these valuations. Future loss emergence may deviate from these estimates. No provision has been made for otherwise unforeseen changes to the legal or economic environment in which claims are settled, nor for causes of loss which are not already reflected in the historical data. Management believes that the techniques employed and assumptions made are appropriate and the conclusions reached are reasonable given the information currently available. Estimates of unpaid grants are reviewed at least annually by an actuary and, as adjustments become necessary, they are reflected in current operations.

4. Accounts Payable and Accrued Liabilities

Included in accounts payable and accrued liabilities is an amount due to the Society's General Fund of \$164,620 (2002 – \$741,558).

5. Comparative Figures

Certain of the prior year's comparative figures have been reclassified to conform to the current year's financial statement presentation.



Management Discussion and Analysis

COMBINED STATEMENT OF REVENUE AND EXPENSES AND SURPLUS

In 2003, the Errors and Omissions Insurance Fund generated an excess of revenue over expenses of \$12.8 million, a decrease of \$5.5 million from 2002. Total expenses increased by \$2.1 million in 2003 and revenues decreased by \$3.4 million to \$103.2 million.

Members' levies

Members' levies increased \$2.1 million in 2003 from \$75 million to \$77.1 million. While the base annual levy for the Ontario professional liability program dropped by \$200 to \$2,500 in 2003, the number of insured members continued to increase.

Other insurance premiums

Other insurance premiums increased to \$9.3 million from \$7.8 million in 2002 as a result of growth in non-mandatory programs including title and excess professional liability insurance.

Reinsurance commissions

LAWPRO earns base commissions on that portion of premium ceded to reinsurers plus additional commissions for profitable results. The decrease of almost \$7.3 million noted in 2003 reflects the discontinuance of reinsurance treaties for the Ontario professional liability and title insurance programs. Because of the improved capital position paired with the unsettled reinsurance market in 2003, LAWPRO chose to assume the risks of these programs, rather than purchase reinsurance as had been done in prior years.

Investment income

The Combined Fund generated \$13.7 million of investment income, an increase of \$0.2 million from the prior year. Typically, over 85% of the investment portfolio consists of debt securities. At year-end, the market value of the portfolio exceeded book value by almost \$10 million (2002- \$2.2 million), largely attributable to recovery in LAWPRO's equity holdings.

Net claims and adjustment expenses

The increase in net claims and adjustment expenses of approximately \$32.2 million is principally due to the change in reinsurance arrangements described above.

Reinsurance premiums

No reinsurance was purchased in 2003 for both the Ontario professional liability and title insurance lines of business. The insurance company continues to fully reinsure the excess professional liability insurance program.

General expenses

The increase in general expenses of \$0.9 million from 2002 levels is primarily attributable to increased compensation and benefits related costs.

COMBINED BALANCE SHEET

Investments

Investment assets, inclusive of cash and cash equivalents, increased by \$27.3 million to \$329.1 million at December 31, 2003 largely a result of the change in reinsurance arrangements for 2003. These additional funds are held to pay future claims. Investment assets are managed in accordance with investment policy in a diversified, high quality portfolio.

Provision for unpaid claims and adjustment expenses and reinsurers' share of provision

The reinsurers' share of the provision for unpaid claims and adjustment expenses decreased from \$133.1 million in 2002 to \$110.9 million in 2003. The decline is due to the transitional effects of ceding lesser portions of the Ontario professional liability program. The percentage ceded dropped in stages from 57 per cent in 1995 to nil in 2003. The provision for unpaid claims, which represents the amount required to satisfy all obligations to claimants without offset for reinsurance, has increased from \$308.5 million in 2002 to \$311.8 million in 2003.

Surplus

The surplus has increased by \$12.8 million, the excess of revenue over expenses for the year.





Auditors' Report

TO THE MEMBERS OF THE LAW SOCIETY OF UPPER CANADA

We have audited the combined balance sheet of THE LAW SOCIETY OF UPPER CANADA – ERRORS AND OMISSIONS INSURANCE FUND as at December 31, 2003 and the combined statements of revenue and expenses and surplus and of cash flows for the year then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these combined financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2003 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario

January 30, 2004

Actuary's Report

For Combined Financial Statements at December 31, 2003

ROLE OF THE VALUATION ACTUARY

The valuation actuary is appointed by the Audit Committee of the Lawyers' Professional Indemnity Company in its capacity as manager of the Law Society of Upper Canada Errors and Omissions Insurance Fund. With respect to the preparation of these combined financial statements, the actuary is required to carry out a valuation of the claims liabilities and to report thereon to the Audit Committee, and through it to the membership of the Law Society. The valuation is carried out in accordance with accepted actuarial practice, and regulatory requirements. The scope of the valuation encompasses the claims liabilities, that is the provision for unpaid claims and adjustment expenses on claims incurred and reported prior to December 31, 2003, the date of these combined financial statements.

In performing the valuation of the liabilities for these future events, which are by their very nature inherently variable, the actuary makes assumptions as to future rates of claims severity, inflation, reinsurance recoveries, expenses and other matters, taking into consideration the circumstances of the Errors and Omissions Insurance Fund, the Lawyers' Professional Indemnity Company and the nature of the insurance coverage being offered. The valuation is necessarily based on estimates, consequently, the final values may vary significantly from those estimates. The actuary also makes use of management information provided by the Law Society and the Lawyers' Professional Indemnity Company, and uses the work of the auditor with respect to the verification of the underlying data used in the valuation.

VALUATION ACTUARY'S REPORT

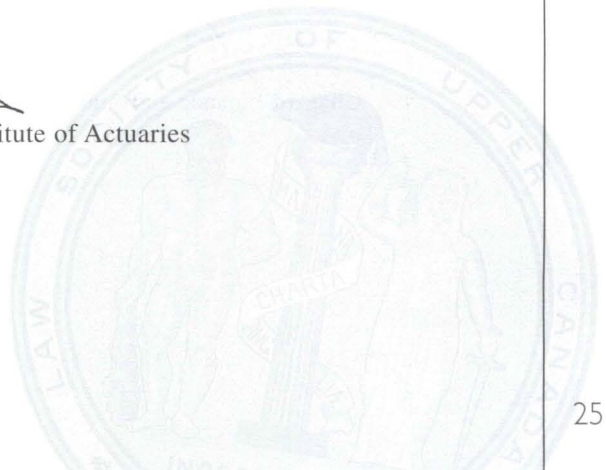
I have valued the claims liabilities arising on the errors and omissions insurance coverage arranged by the Law Society of Upper Canada for its Errors and Omissions Insurance Fund combined balance sheet as at December 31, 2003, and their changes in its combined statement of revenue and expenses and surplus for the year then ended, in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amount of the claims liabilities makes appropriate provision for all such obligations, and the financial statements fairly present the results of the valuation.



Brian G. Pelly
Fellow, Canadian Institute of Actuaries

Toronto, Ontario
January 30, 2004





Combined Balance Sheet

Stated in thousands of dollars

As at December 31

	2003	2002
ASSETS		
Cash and cash equivalents	9,877	2,786
Investments (note 5)	319,186	299,016
Investment income due and accrued	2,539	3,273
Accounts receivable	12,570	15,803
Reinsurers' share of provision for unpaid claims and adjustment expenses (note 7)	110,866	133,082
Other receivables	1,292	1,110
Other assets	320	134
Fixed assets (accumulated depreciation 2003 – 4,898; 2002 – 4,203)	1,076	1,454
Future income taxes (notes 2 and 3)	4,230	465
Total assets	461,956	457,123
LIABILITIES AND SURPLUS		
Provision for unpaid claims and adjustment expenses (notes 4 and 7)	311,788	308,520
Premium stabilization fund (note 9)	20,431	25,831
Accounts payable and accrued liabilities	6,684	12,497
Surplus (note 6)	123,053	110,275
Total liabilities and surplus	461,956	457,123

See accompanying notes

On behalf of Convocation:

Treasurer

Chair of Finance and Audit Committee

Combined Statement of Revenue and Expenses and Surplus

Stated in thousands of dollars

<i>Year Ended December 31</i>	2003	2002
REVENUE		
Members' levies, mandatory insurance program (<i>notes 8 and 9</i>)	77,123	75,014
Other insurance premiums	9,313	7,773
Reinsurance commissions	3,073	10,343
Investment income	13,691	13,444
Total revenue	103,200	106,574
EXPENSES		
Net claims and adjustment expenses (<i>notes 4 and 7</i>)	65,142	32,927
Reinsurance premiums	4,527	31,520
General expenses	11,708	10,812
Transfer to Law Society General Fund (<i>note 10</i>)	3,000	2,600
Premium taxes	2,619	2,498
Provision for income taxes (<i>note 2</i>)	3,426	7,941
Total expenses	90,422	88,298
Excess of revenue over expenses	12,778	18,276
Surplus, beginning of year	110,275	91,999
Surplus, end of year	123,053	110,275

See accompanying notes





Combined Statement of Cash Flows

Stated in thousands of dollars

Year Ended December 31

	2003	2002
OPERATING ACTIVITIES		
Excess of revenue over expenses	12,778	18,276
Items not affecting cash:		
Depreciation	695	605
Future income taxes	(3,765)	1,374
Realized gains	(763)	(646)
Amortization of discount on bonds	(2,046)	(1,262)
	6,899	18,347
Other operating sources (uses) of cash:		
Investment income due and accrued	734	(308)
Amounts receivable and other assets	2,865	(2,762)
Reinsurers' share of provision for unpaid claims and adjustment expenses	22,216	10,946
Provision for unpaid claims and adjustment expenses	3,268	(20,598)
Premium stabilization fund	(5,400)	(772)
Accounts payable and accrued liabilities	(5,813)	350
Total funds provided by operating activities	24,769	5,203
INVESTING ACTIVITIES		
Fixed assets:		
Purchase of fixed assets	(317)	(1,437)
Investments:		
Purchases of investments	(872,532)	(189,092)
Proceeds from sale of investments	855,171	180,083
Investment purchases, net	(17,361)	(9,009)
Total funds provided by investing activities	(17,678)	(10,446)
Net change in cash and cash equivalents	7,091	(5,243)
Cash and cash equivalents, beginning of year	2,786	8,029
Cash and cash equivalents, end of year	9,877	2,786

See accompanying notes

Notes to Combined Financial Statements

As at December 31, 2003

(Stated in whole dollars except where indicated)

1. The Insurance Program and its Risk Retention and Reinsurance Structure

The combined financial statements of the Errors and Omissions Insurance Fund ("the Combined Fund") account for the net results of the professional liability insurance program of the Law Society of Upper Canada ("the Society"). The program requires practising members to pay annual levies to fund the anticipated costs of professional liability claims made in each annual policy period. Indemnification of members is subject to the terms of the insurance policy, including financial limits per claim and aggregate limits per member in each policy period.

These financial statements combine the results of operations, financial positions and cash flows of:

- the Errors and Omissions Insurance Fund of the Society ("the Fund"), the fund originally set up in the Society's accounts to record insurance claims and expenses and related levies and their investments; and
- Lawyers' Professional Indemnity Company ("LAWPRO"), a wholly owned subsidiary of the Society that was incorporated in 1990 as an insurance company and is licensed to provide lawyers' professional liability and title insurance.

The risk retention and reinsurance structures employed through these two entities are described in the following paragraphs.

Prior to July 1, 1990, the Society's Errors and Omissions Insurance Program was underwritten by various insurance carriers subject to a policy deductible. LAWPRO took over the underwriting of the program commencing July 1, 1990. The Society maintained financial responsibility for the policy deductible through to December 31, 1994. The policy deductible was a combination of a group deductible and the individual member deductibles. For the periods noted below, the combined policy deductibles were as follows:

July 1989 to June 1990	\$ 250,000 per occurrence
July 1990 to December 1991	\$ 200,000 per occurrence
January 1992 to December 1994	\$ 250,000 per occurrence

The Society was not able to arrange Stop Loss reinsurance on its group deductible after the policy period ending June 1989. As a result, the full financial risk of the deductible rested with the Society, from July of 1989 through the policy period ended December 1994.

LAWPRO also had a net retention above the policy's group deductible as follows:

- July 1, 1990 to December 31, 1991: LAWPRO is liable for \$50,000 of all individual losses in excess of \$200,000;
- January 1, 1992 to December 31, 1992: LAWPRO is liable for an aggregate of \$2,500,000 from individual losses incurred in excess of \$250,000 plus a further 10% of all losses above \$250,000 once the initial \$2,500,000 limit has been reached; and
- January 1, 1993 to December 31, 1994: LAWPRO is liable in each policy year for an aggregate of \$4,000,000 if incurred losses are above or exceed \$250,000 plus a further 10% of all losses in excess of \$250,000 once the initial \$4,000,000 limit has been reached.



It was decided, effective January 1, 1995, to eliminate the self-insured group deductible. Commencing January 1, 1995, 100% of the risk over the individual member deductibles is insured within LAWPRO. LAWPRO in turn reinsures a portion of its risk retention with third party Canadian licensed reinsurers. The policy limits for the period January 1, 2003 through December 31, 2003 are \$1 million per claim and \$2 million per member in aggregate.

2. Significant Accounting Policies

These combined financial statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP). The most significant accounting policies are as follows:

Members' Levies, Mandatory Insurance Program and Other Insurance Premiums

Members' levies are recorded when billed with the exception of those based on transactions. The transaction levy, first introduced in 1995, is recorded on a cash basis based on members' filings.

Other Insurance Premiums represent revenues generated from non-mandatory programs including title insurance and excess professional liability coverage. These transactions are recorded as revenue on an issued basis.

Investments

Investments in debt securities are recorded at amortized cost. Premiums and discounts from par value are amortized on a straight-line basis over the term to maturity. Investments in common or preferred shares are carried at cost. Gains and losses on investments are included in investment income when realized. Any losses in value of an investment, which are considered other than temporary in nature, are recognized in income.

Fixed assets

Fixed assets are presented at cost, net of accumulated depreciation and amortization. Depreciation and amortization are charged to expense on a straight-line basis over the estimated useful lives of the assets as follows:

Leasehold improvements	Term of lease
Furniture and equipment	3 to 5 years
Software	1 to 3 years

Claims related balances

a) Provision for unpaid claims and adjustment expenses

The insurance program covers claims made against insureds in the policy period.

The provision is determined using case-basis evaluations plus an amount for future development and delayed reporting and is an estimation of the ultimate discounted cost of all insurance claims to December 31, 2003. The estimates are regularly reviewed and updated and any resulting adjustments are included in current income.

The provision for unpaid claims is presented net of a discount that reflects an estimation of the investment income that will be earned on funds until they are paid out in settlement of claims. Accordingly, the provision as recorded represents fair value. The estimation of the discount is based on anticipated investment rates of return and experience with payout patterns on similar types of claims.

b) Reinsurers' share of provisions for unpaid claims and adjustment expenses

Expected reinsurance recoveries on unpaid claims and adjustment expenses, are recognized as assets at the same time as, and using principles consistent with the Society's method for establishing the related liability.

c) Members' Deductibles

The insurance policy calls for insured members to pay deductibles, which range from nil up to \$25,000. Expected deductible recoveries on paid and unpaid claims are recognized net of any required provision for uncollectible accounts, using principles consistent with the Combined Fund's method for establishing the related claims liability.

Income taxes

LAWPRO uses the asset and liability method of accounting for income tax purposes. Under the asset and liability method of tax allocation, future income tax assets and liabilities are determined based on the differences between the financial reporting and tax basis of assets and liabilities, and are measured using the substantively enacted tax rates and laws that are expected to be in effect in the periods in which the future income tax assets or liabilities are expected to be settled or realized.

The Fund is not subject to income or capital taxes because it is a not-for-profit corporation.

3. Change in Accounting Policy

In accordance with GAAP, claims are reflected on the Combined Financial Statements on a discounted basis. In 2002 and prior years, the LAWPRO stand alone statements issued for insurance regulatory purposes were prepared on an undiscounted basis and restated for combination purposes.

Effective January 1, 2003, in accordance with the insurance regulator's requirements, LAWPRO has implemented a change in accounting policy whereby loss provisions for unpaid claims are disclosed on a discounted or fair value basis. The change in accounting policy has the effect of decreasing the 2002 balance of future income tax asset and surplus by \$3.6 million.

4. Measurement Uncertainty

The settlement of professional liability claims involves processes, the outcome of which is inherently uncertain. Consequently, the estimation of the ultimate settlement costs of claims made to date, that underlies the provision for unpaid claims and adjustment expenses, involves measurement uncertainty. The amounts are necessarily based on estimates of future trends in claim severity and other factors, which could vary as the claims are settled. Ultimate costs incurred will inevitably vary from current estimates, to some extent. Although it is not possible to measure the degree of variability inherent in such estimates, management believes that the provision for unpaid claims and adjustment expenses is adequate. Estimates are reviewed at least annually by an actuary and, as adjustments to these liabilities become necessary, they are reflected in current operations.

There is also measurement uncertainty inherent in the estimation of reinsurance recoveries and members' deductible recoveries. Management is satisfied that appropriate provisions have been made for potentially unrecoverable amounts and believes that any remaining exposure would prove immaterial to these financial statements.



5. Investment Information

The Fund and LAWPRO hold a diversified portfolio consisting of equities and fixed income securities with investment grades of "A" or better.

Estimated fair values

The book values and estimated fair values on investments as at December 31 were as follows:

(000's)	2003			2002		
	Book value	Estimated fair value	Yield %	Book value	Estimated fair value	Yield %
Debt Securities	285,790	290,690	4.3	258,629	264,878	4.2
Common Shares	28,540	33,448		32,542	28,454	
Preferred Shares	4,856	5,035		7,845	7,869	
	319,186	329,173		299,016	301,201	

The estimated fair values of debt securities, common and preferred shares are based on quoted market values.

Liquidity and interest rate risk

The maturity profile of debt securities as at December 31, 2003 is as follows:

(000's)	Within 1 year	1 to 5 years	Over 5 years	Book value
Debt securities	9,990	180,831	94,969	285,790
Per cent of total	4%	63%	33%	

The average duration of debt securities at December 31, 2003 is 3.8 years. LAWPRO attempts to match the maturity of these investments to the expected maturity of claims obligations. Shares have no specific maturities.

6. Surplus

The Surplus of the Combined Fund includes LAWPRO's capital and surplus. At December 31, 2003 the Statutory Capital, Surplus and Reserves of LAWPRO, as reported under insurance regulatory requirements, was \$96.2 million (2002 – \$88.7 million).

7. Claims and Adjustment Expenses

Reinsurance Ceded

To limit losses through the spreading of risks, the Fund and LAWPRO cede reinsurance with other insurers.

Net claims and adjustment expenses presented in the combined statement of revenue and expenses and surplus are net of reinsurance ceded in the amounts of \$3.0 million (2002 – \$19.9 million).

In the event that a reinsurer is unable to meet obligations assumed under reinsurance agreements, the Fund and LAWPRO are liable for such amounts.

8. Members' Levies, Mandatory Insurance Program

Members' levies for the 2003 year include annual base levies of \$2,500 per member (2002 – \$2,700) and additional levies that are charged based on a member's claims history, status, and certain reported transaction volumes. In 2003, additional levies totalled \$26.6 million (2002 – \$26.4 million). The balances are shown net of the retrospective premium rating adjustment.

9. Premium Stabilization Fund

Revenues from transaction based levies are subject to variation in levels of legal transactions that, in part, reflect the changing economic climate. Any revenues from transaction and claims history levies that are in excess of premium levels agreed for the year, are held for future insurance purposes and applied as premiums under the insurance program in future years. Should a shortfall in these levies be experienced, the deficiency in funds shall be transferred from the Premium Stabilization Fund. The amount drawn down in 2003 was \$6.1 million (2002 – \$4.9 million).

Further, this fund also reflects retrospective premium rate adjustments under the insurance agreement between the Society and LAWPRO. The Premium Stabilization Fund was augmented by \$0.7 million in 2003 through this adjustment (2002 – \$4.1 million).

10. Transfer to Law Society General Fund

Investment income revenues of the stand-alone Fund totalling \$3.0 million (2002 – \$2.6 million), which were determined to be in excess of operating requirements, were transferred to the Society for general purposes.

11. Commitments

LAWPRO is committed to monthly lease payments in effect until January 31, 2008. Lease payment obligations are as follows:

2004	\$1,362,000
2005	\$1,362,000
2006	\$1,362,000
2007	\$1,362,000
2008	\$ 114,000



Management Discussion and Analysis

LibraryCo Inc. is mandated to carry on the central management of the Ontario County and District Law Library system on a not-for-profit basis in accordance with the objectives of the *Blended System* framework for the purpose of developing and enhancing skills for the “competent lawyer” in Ontario.

STATEMENT OF REVENUES AND EXPENSES

Total revenues were consistent with 2002, approximating \$6.7 million. LibraryCo’s short term financial plans include budgeting to utilize funds from the Reserve Fund. In 2003, \$150,000 (2002 – \$50,000) was transferred from the Reserve Fund to offset the excess of operating expenses over revenues.

Revenues

The \$6.7 million total revenues in 2003 consisted of grants of \$5.8 million (2002 – \$5.4 million) from the Law Society and \$850,000 (2002 – \$1.3 million) from the Law Foundation of Ontario. The 2003 County Library levy collected by the Law Society was \$195 per member (2002 – \$208) with membership numbers increasing and \$323,000 also being transferred from the General Fund’s County Library restricted fund.

Expenses

Like 2002, expenses required for the operation of the 48 County and District law libraries make up \$6.4 million of the total \$6.8 million in expenses. These expenses are primarily for collections – traditional and electronic, personnel and operations. LibraryCo continues to balance the demand for materials from the various libraries and to provide education in the use of these materials. LibraryCo is also striving to maintain the balance between traditional and electronic resources and therefore to make reliable, relevant, current and historic legal information accessible to all County and District law libraries.

The mix of expenses is consistent with prior years. \$403,000 (2002 – \$366,000) was spent on head office operations and administration of the library system. The position of Roving Law Librarian was in place for the full 2003 year.

BALANCE SHEET

There were no significant changes in balance sheet categories or values during the year. The Reserve Fund of \$1.7 million (2002 – \$1.8 million) is restricted for County and District law library purposes as approved by the Board of Directors.

Auditors' Report

TO THE SHAREHOLDERS OF LIBRARYCO INC.:

We have audited the balance sheet of LIBRARYCO INC. as at December 31, 2003 and the statements of revenue and expenses, changes in fund balances and cash flows for the year then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Organization as at December 31, 2003 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario
January 30, 2004





Balance Sheet

Stated in dollars

As at December 31

	2003	2002
CURRENT ASSETS		
Cash and short-term investments	1,652,658	1,469,229
Prepaid expenses	18,778	15,304
Goods and Services Tax receivable	37,450	83,821
Due from Law Foundation of Ontario	—	322,500
	1,708,886	1,890,854
CAPITAL ASSETS (note 4)	21,957	29,601
Total Assets	1,730,843	1,920,455
LIABILITIES, SHARE CAPITAL, AND FUND BALANCES		
Accounts payable and accrued liabilities (note 3)	34,628	111,848
SHARE CAPITAL AND FUND BALANCES		
Share capital (note 5)	200	200
General fund	(17,841)	(22,479)
Invested in capital assets fund	21,957	29,601
Reserve fund	1,691,899	1,801,285
Total Share Capital and Fund Balances	1,696,215	1,808,607
Total Liabilities, Share Capital and Fund Balances	1,730,843	1,920,455

See accompanying notes

On behalf of the Board of Directors

Gregory M. Muligan

Chair – Board of Directors

Richard G. Urban

Chair – Finance Committee

Statement of Revenues and Expenses

Stated in dollars

For the year ended December 31

	2003	2002
REVENUES		
Law Society of Upper Canada grant	5,794,650	5,408,000
Law Foundation of Ontario grant	850,000	1,290,000
Interest income	40,614	25,249
Total revenues	6,685,264	6,723,249
EXPENSES		
Head office/administration		
Salaries and benefits	210,057	169,476
Office and occupancy	58,295	53,388
Professional fees	50,891	76,585
Other (note 6)	83,652	66,328
Total head office/administration expenses	402,895	365,777
County and District Law Libraries – centralized purchases		
Electronic products and services	1,397,039	1,090,355
Hardware/software upgrades	–	154,645
Ergonomic furnishings	–	45,000
Insurance and group benefits	184,380	209,738
Other (note 7)	208,303	144,503
	1,789,722	1,644,241
County and District Law Libraries – grants (note 8)	4,605,039	4,736,432
Total County and District Law Libraries expenses	6,394,761	6,380,673
Total expenses	6,797,656	6,746,450
Excess of expenses over revenue for the year	(112,392)	(23,201)

See accompanying notes





Statement of Changes in Fund Balances

Stated in dollars

For the year ended December 31

	2003				2002
	General Fund	Invested in Capital Assets Fund	Reserve Fund	Total	Total
Balance, beginning of year	(22,479)	29,601	1,801,285	1,808,407	1,831,608
Excess of (expenses over revenue)					
revenue over expenses	(145,362)	(7,644)	40,614	(112,392)	(23,201)
Inter-fund transfer	150,000	—	(150,000)	—	—
	(17,841)	21,957	1,691,899	1,696,015	1,808,407

See accompanying notes

Statement of Cash Flows

Stated in dollars

For the year ended December 31

	2003	2002
OPERATING ACTIVITIES		
Excess of expenses over revenue	(112,392)	(23,201)
Item not affecting cash		
Amortization of capital assets	7,644	9,745
Net change in working capital items		
Prepaid expenses	(3,474)	(7,105)
Goods and Services Tax receivable	46,371	(81,034)
Due from Law Foundation of Ontario	322,500	(322,500)
Accounts payable and accrued liabilities	(77,220)	53,581
Total operating activities	183,429	(370,514)
FINANCING ACTIVITIES		
Advances to related party	—	13,427
Increase (decrease) in cash	183,429	(357,087)
Cash and short-term investments, beginning of year	1,469,229	1,826,316
Cash and short-term investments, end of year	1,652,658	1,469,229

See accompanying notes





Notes to Financial Statements

For the year ended December 31, 2003

(Stated in whole dollars except where indicated)

1. General

LibraryCo Inc. (the “organization”) is a wholly owned, not-for-profit subsidiary of the Law Society of Upper Canada, incorporated on April 12, 2001 under the *Ontario Business Corporations Act*. The Law Society of Upper Canada holds all common shares of the organization and the County and District Law Presidents’ Association holds all special shares.

The purpose of the organization is to administer funding from the members of the Law Society of Upper Canada and develop policies, priorities, guidelines and standards for the delivery of county law library services across Ontario including the distribution of funds to the various County and District Law Libraries.

As a not-for-profit organization, LibraryCo Inc. is not subject to federal and provincial income and capital taxes.

2. Significant Accounting Policies

Basis of presentation

The financial statements have been prepared in accordance with the accounting standards for non-profit organizations published by the Canadian Institute of Chartered Accountants, using the restricted fund method of reporting contributions.

The General Fund accounts for the delivery, management and administration of library services. The Reserve Fund is restricted for specific purposes as periodically determined and approved by the Board of Directors. The Invested in Capital Assets Fund records the capital assets of the organization.

Cash and short-term investments

Cash and short-term investments are amounts on deposit and invested in short-term (less than one year) investment vehicles according to the organization’s investment policy. Short-term investments are stated at the lower of cost and market value. Investment income, except income earned on General Fund resources, is retained in and reported by the Reserve Fund.

Capital assets

Capital assets are presented at cost net of accumulated amortization. Amortization is charged to expenses on a declining balance basis as follows:

Furniture and fixtures	20%
Computer equipment	30%
Leasehold improvements	Straight-line over term of lease

In the year of acquisition, half the normal amortization is provided.

Computer software is expensed in the year of acquisition.

Revenue recognition

Restricted contributions related to the general operations are recognized as revenue of the General Fund in the year in which the related expenses are incurred. All other restricted contributions are recognized as revenue of the appropriate restricted fund.

Collections

The organization owns a collection of traditional, and electronic based, legal research and reference material. The cost of additions to the collection is expensed as incurred.

Financial instruments

The estimated fair value of cash and short-term investments, accounts receivable, prepaid expenses, accounts payable and accrued liabilities approximates their carrying amounts in the financial statements due to the relatively short period to maturity of these instruments.

Measurement uncertainty

The preparation of the financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingencies at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Related Party Transactions and Balances

	2003	2002
<i>Transactions</i>		
Purchases from the Law Society of Upper Canada	\$ 93,292	\$ 84,853
<i>Balances</i>		
Amount due to the Law Society of Upper Canada (included in accounts payable and accrued liabilities)	\$ 7,680	\$ 82,883

Included in purchases from the Law Society of Upper Canada are costs associated with cataloguing of collections, CLE and Bar Admission Course materials for the County & District Law Libraries and catering for Board of Directors' meetings.

4. Capital Assets

	2003		2002
	Cost	Accumulated amortization	Net
Furniture and fixtures	\$15,938	\$ 6,758	\$ 9,180
Computer equipment	19,962	11,648	8,314
Leasehold improvements	8,927	4,464	4,463
	\$44,827	\$22,870	\$21,957
			\$29,601



5. Share Capital

Authorized

Unlimited number of Common shares

Unlimited number of Special shares, with right to elect one director

Issued	2003	2002
100 Common shares	\$100	\$100
100 Special shares	100	100
	\$200	\$200

At incorporation, the organization issued 100 Common shares to the Law Society of Upper Canada and 100 Special shares to the County & District Law Presidents' Association for cash consideration of \$100 each.

6. Other Expenses – Head Office/Administration

Included in this expense are costs associated with staff travel, Board of Directors' meetings and other miscellaneous items.

7. Other Expenses – County and District Law Libraries – Centralized Purchases

Included in this expense are costs associated with publications, cataloguing, committee meetings, special needs, and other miscellaneous items.

8. County and District Law Library Grants

These grants represent the quarterly distribution of funds to the 48 County and District Law Libraries. These grants are distributed in accordance with policies and procedures as established by the organization's Board of Directors.

In order to satisfy themselves as to the proper use of these funds, management has undertaken the following procedures:

Periodic visits, by the organization's staff, to the individual libraries to review financial information, assess collections, and to determine services being provided;

Submission of annual budgets by each individual library and review of these budgets by the organization's staff;

Submission of periodic financial information by each individual library and review of this information by the organization's staff;

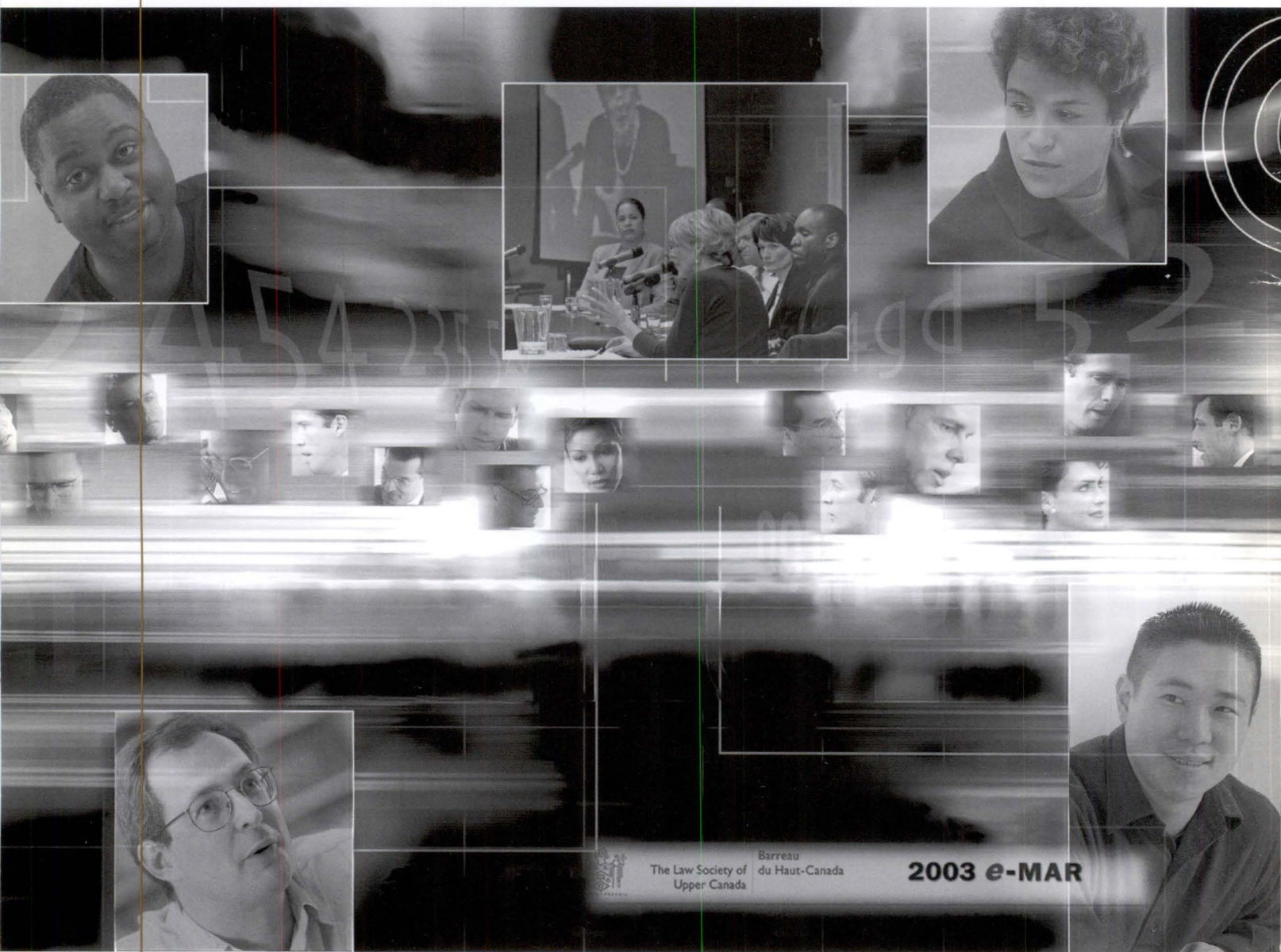
Annual conference with the organization's staff and staff of all individual libraries.

The following individual library grants were distributed by the organization during 2003 and 2002:

	2003	2002
Algoma District Law Association	\$ 71,000	\$ 82,372
Brant Law Association	62,000	74,136
Bruce Law Association	45,600	55,696
County of Carleton Law Association	483,000	399,748
Cochrane Law Association	55,000	90,452
Dufferin Law Association	42,200	52,572
Durham County Law Association	96,000	111,824
Elgin Law Association	52,200	60,136
Essex Law Association	204,160	168,036
Frontenac Law Association	108,000	73,992
Grey Law Association	52,000	55,996
Haldimand Law Association	34,500	51,148
Halton Law Association	97,900	109,376
Hamilton Law Association	286,000	272,968
Hastings Law Association	64,000	76,064
Huron Law Association	56,000	54,564
Kenora Law Association	62,000	62,884
Kent Law Association	44,000	55,392
Lambton County Law Association	46,000	58,352
County of Lanark Law Association	34,000	54,312
Leeds & Grenville Law Association	48,000	59,032
Lennox & Addington Law Association	21,000	50,828
Lincoln Law Association	125,500	130,504
Manitoulin Law Association	5,500	5,400
Metropolitan Toronto Lawyers Association	459,000	413,216
Middlesex Law Association	260,000	232,692
Muskoka Law Association	37,000	53,204
Nipissing Law Association	57,000	69,328
Norfolk Law Association	49,000	54,196
Northumberland County Law Association	47,368	54,760
Oxford Law Association	54,000	55,368
Parry Sound Law Association	30,000	43,060
Peel Law Association	225,000	172,000
County of Perth Law Association	42,000	47,476
Peterborough Law Association	78,000	82,460
Prescott & Russell Law Association	33,000	49,308
Rainy River Law Association	38,000	51,916
Renfrew County Law Association	85,000	77,536
County of Simcoe Law Association	115,000	118,156
Stormont, Dundas & Glengarry Law Association	54,000	56,300
Sudbury District Law Association	109,000	122,344
Temiskaming Law Association	39,000	54,360
Thunder Bay Law Association	120,000	110,880
Victoria Haliburton Law Association	58,000	71,940
Waterloo Law Association	170,611	174,476
Welland Law Association	65,000	91,396
Wellington Law Association	59,500	91,952
York Region Law Association	125,000	122,324
	\$4,605,039	\$4,736,432

9. Lease Commitments

The organization has entered into a lease arrangement for its offices. The lease term is five years, expiring July 31, 2006 and requires annual payments of \$10,992 plus operating costs for the first three years and \$13,200 plus operating costs for the last two years.



The Law Society of
Upper Canada

Barreau
du Haut-Canada

2003 e-MAR

Osgoode Hall
130 Queen Street West
Toronto, Ontario M5H 2N6
416-947-3300
1-800-668-7380
www.lsuc.on.ca

